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Written Testimony

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Mr. Chairman and members of the committee, I am Tom Camerlo, Chairman of the National Milk Producers Federation (NMPF), Dairy Farmers of America and the Trade Policy Committee of the U.S. Dairy Export Council. The National Milk Producers Federation works closely with the U.S. Dairy Export Council (USDEC) on issues of trade policy. I am pleased to appear before you today to testify on the topic of negotiations in the World Trade Organization and bilateral and regional agreements.

America's dairy industry is the second largest agricultural commodity sector in the United States, measured by farm cash receipts. The 85,000 dairy farmers in the U.S. are in every state of the Union, from Vermont to California, New Mexico to Idaho. Dairy is one of the top three agricultural sectors in fully half the states, and almost two-thirds of the members of the House hail from one of these "dairy" states. Internationally, the U.S. is the world's largest single-country producer of cow's milk.

Impressive as those numbers are, they represent only the milk producer side of the industry; dairy processors, the companies that turn milk into yogurt, cheese, ice cream and milk powder, add overall strength and employment to the impact of the industry as a whole on the country's economy. In addition, we know that our ability to increase production, impacting employment in both producing and processing sectors, is almost unconstrained. This makes our efforts to market U.S. dairy products for export all the more important to the industry and to this country's overall rural economy. However, these efforts will be meaningless if the United States becomes the dumping ground for heavily subsidized products from countries with small markets. We cannot continue down the road of unilateral disarmament. Markets need to be opened overseas before we open ours further.

The World Trade Organization -- Doha Development Round

As its title states, the Doha development round has been characterized as a catalyst for developing countries to achieve greater economic opportunities. In that vein, the United States government and the dairy industry are poised to accomplish those objectives through further trade reform. The U.S. dairy industry has been a proponent of harmonizing tariffs, eliminating export subsidies and reducing domestic support in a manner that will not leave U.S. producers at a competitive disadvantage as compared to other developed countries. The United States government has also pursued these general principles as it presented its proposal at the agricultural negotiations of the World Trade Organization.

An overall analysis of the Harbinson paper approach to the three pillars and its impact on dairy has shown significant flaws. The Harbinson paper regrettably achieves harmonization neither on market access nor in domestic support. In fact, the Harbinson paper as it stands today would only slightly reduce the level of disparities which exist under the Uruguay Round. In fact, Harbinson's proposals would create an even worse scenario by reducing the already low tariffs (e.g. U.S. dairy) even further while allowing for other countries to maintain three digit levels of protective tariffs. Likewise, the Harbinson paper could permit the EU to begin reducing their domestic support from a significantly higher point than the United States, thus leaving the current inequities in place.

The Three Pillars
The U.S. dairy industry has built its trade priorities around the proposition that the playing field must be leveled and inequities eliminated. Our dairy sector can compete internationally, but only if distortions disappear in a fair manner and not unilaterally. The United States Congress needs to carefully examine the pros and cons of an agreement that goes beyond the three "pillars".

Export Subsidies
The U.S. dairy industry has stated numerous times that is willing to give up the Dairy Export Incentive Program as long as the Europeans and others eliminate their export subsidies entirely. In fact, we believe the pervasively negative effect of export subsidies is so extensive that the U.S. industry's competitiveness in world markets will improve given rapid elimination of export subsidies. The majority of WTO members have already identified the complete elimination of export subsidies as a goal.

The Doha Ministerial mandated the Chairman of the Agriculture negotiating group (Stuart Harbinson) to produce a modalities paper (principles for negotiating) by March 31st, 2003. In order to meet the deadline, Mr. Harbinson produced a modalities paper that seemingly was intended to represent in some form the views of member countries. However, the Harbinson modalities paper currently under review by WTO member countries is not ambitious enough. Inasmuch as it calls for the elimination of all export subsides, the nine year period allowed for this elimination is too long. Globally, dairy industries are the largest recipients of export subsidies, with the European Union (EU) holding nearly 72 percent of all export subsidy allowances in dairy. The EU has significant levels of export subsidies available in commodities other than dairy. Allowing countries such as the EU to maintain export subsidies for a longer period for certain products (e.g. dairy) in exchange for eliminating the subsidies on other commodities at a faster rate would be devastating for our industry and should not be considered a viable avenue.

State Trading Enterprises (STEs) do not necessarily constitute interference to trade. An example of a properly structured entity is the Commodity Credit Corporation (CCC) in the United States. However, monopolistic STEs, receiving preferential treatment with respect to exports and imports, have consistently distorted trade. The Doha Round must not allow State Trading Enterprises, or companies sanctioned by the government to have exclusive rights to all domestic milk as well as exclusive rights to export markets, to continue to function. Any elimination of export subsidies should address the enormous distortions created by STE organizations.

Although the industry is a relative newcomer to international trade, and such trade is still modest in comparison to the size of the domestic market, the United States exported approximately 5 percent of its domestic milk production in 2001. Exports amount to roughly 8 percent if one removes fluid drinking milk, which is difficult to export due to its perishable nature. More importantly, our export share for cheese has grown more quickly in recent years than traditional and heavily subsidized exporters such as Europe, and at about the same rate as low cost producer countries such as New Zealand. America's share of exported production on a milk solids basis has generally been growing over the past five, typically keeping pace with the steady increases in production that have marked the industry's historical trends.

In fact, the United States exported over $1 billion in assorted dairy products in 2002; the third consecutive record-breaking year of foreign sales. Despite this impressive number, the U.S. is only fourth in the world in dairy exports. This status reflects both the industry's recent turn from its inward focus, as well as the often hostile world dairy trade environment that is beset with price depressing export subsidies and high market access barriers. If the next WTO round eliminated all export subsidies, the EU would lose a significant tool to export at sub-market prices:

- Approximately 78% of last year's exports of 458,500 metric tons of cheese, or about 35% of total world trade.
- Approximately 80% of last year's exports of 358,000 metric tons of SMP, or about 24% of total world trade.
- Approximately 60% of last year's exports of 131,000 metric tons of butter, or about 12% of total world trade.

Market Access

NMPF values export markets and the potential for expanding those markets. However, poorly negotiated WTO terms will dramatically affect U.S. dairy farmers and the U.S. industry as a whole. Therefore, our market access objectives focus on leveling the playing field and ensuring that the United States does not continue to provide greater access than other member countries.

Market access is perhaps the most important aspect of the negotiations for U.S. dairy producers. But unlike many who prioritize this issue, the U.S.'s position does not result from a trade adverse stance, but rather from an aggressive pursuit of trade reform.

Contrary to what many in this committee and in the media may believe, the U.S. dairy industry imports large quantities of non-quota products, as well as a significant amount of products above and beyond their quota limits. During the 1999 to 2001 time period, out of a total of 805 million lbs. per year, 65 percent of that amount came from non-quota products. During those years, the U.S. also imported 55 million lbs. per year of over-quota products, an additional amount equating to roughly 25 percent of the in-quota product imports. Unfortunately, the commitments in the last WTO round permitted many members to isolate their markets entirely, beyond the negotiated minimum access, while countries like the United States provided significantly more net access.

Since the Uruguay Round, over-quota imports have severely affected the United States because of our relatively low over-quota tariffs when compared to other protected markets. Therefore, the industry's priority is the harmonization of tariffs, especially over-quota tariffs. Final Uruguay Round bound tariff levels on key dairy products are still in excess of 50 percent for many WTO members, while the U.S. in-quota rates are nearly or simply zero. Likewise, the average U.S. over-quota tariff for dairy products is about 52 percent, while the average over-quota dairy tariff in the EU, Canada, Japan, Korea and other countries typically remains well into the triple digits.

U.S. companies strongly believe we can be competitive in many dairy categories if given a truly level playing field. To this end, the United States should concentrate on the reduction and harmonization of high tariffs, while improving the administration and enforcement of tariff rate quotas. Because the Uruguay Round accomplished important but very limited access improvements for U.S. dairy products; without another round of market access reform, we cannot negotiate viable commercial access for U.S. dairy products to many important markets, as well as address the issue of peak tariffs around the world. Most importantly, the pace of reforms in market access should be linked to the timetable on export subsidy elimination.

We oppose any additional in-quota access unless export subsidies are eliminated and over-quota tariffs are harmonized. Furthermore, considerations of additional in-quota access should also take into consideration the net trade flows through over-quota access. Also, if agreed, additional in-quota access should be given first to developing countries and to those countries that did not enjoy special country allocations (e.g. the United States) during the Uruguay Round. Any access that benefits European or other OECD countries should be compensated for with a specific country allocation for U.S. dairy products into those markets.

Finally, it is necessary to ensure that the United States does not provide more access (in-quota or over-quota) than any other protective world market, particularly in ways that put our industry at a competitive disadvantage. Because of the disparities created by the Uruguay Round peak tariffs, it is essential that the market access modalities include a system to evaluate the actual over-quota access that each protected market offers. In other words, calculations of minimum market access should also consider both in-quota access as well as over-quota access when calculating any further concessions. Dairy producers will re-evaluate their support of the Doha Round if the method chosen for reducing tariffs forces the United States to open its markets while other WTO members are permitted to maintain high levels of tariff protection.

The continuation of safeguards is essential to remedying price depressing import surges of dairy products. Although we understand the danger of improperly stifling access to foreign markets, a transparent, quick and efficient safeguard, with specific disciplines that address import surges, is extremely important. The special safeguard provisions adopted in previous negotiations have not proven to be very effective and need modification towards transparency and simplicity. The U.S. government needs to be able to implement these safeguards without delay.

Domestic Support

With respect to domestic supports we support the expansion of the green box principles, which do not distort trade. The green box principles should be maintained and expanded to include programs that allow producers to support themselves with and without taxpayers' money.

In general, we support the U.S. government's proposal of an exempt and non-exempt approach to subsidies. However, the elimination of the blue box should not be accepted as a condition for the EU to maintain the current huge disparities under the amber box. The elimination of inequities under the blue and amber boxes is a high priority for the U.S. dairy industry and should be addressed in the negotiations on agriculture. We do not support the elimination of these programs. Moreover, the United States should only accept reductions in domestic support as part of a package that includes elimination of export subsidies and reciprocal market access. Unless negotiations reduce serious disparities in the levels of government support and offer significant market access in all countries, developed and developing, the United States must continue internal programs that counter heavy subsidization by Europe and other OECD members.

The Farm Bill of 2002 authorized the price support program for another seven years. Under the WTO's nomenclature for agricultural domestic support, the price support program is considered classified in the "amber box" category with most trade distorting systems. We believe that the current WTO rules of notification regarding the amber box that emanated from the Uruguay Round, under which the U.S. price support program operates, have significant flaws.

The most obvious oversight is the double counting of producer support. For instance, the U.S. price support program had little impact on U.S. dairy prices until 1999. Nevertheless, the United States notified to the WTO an average of $4.5 billion annually for dairy price support, when in reality government outlays were near zero.

Non-trade concerns

In addition to the three pillars of U.S. dairy trade concerns (export subsidies, market access and domestic support), the issues of non-trade concerns (geographical indications, the precautionary principle, labeling and food safety), as well as the topic of special and differential treatment for developing countries, have the potential for severely damaging the future of dairy trade reform.

The EU commission has begun a rampant process to expand the types of products given special protection by so-called "geographical indications" (GIs). Domestically, the EU recently proposed changes in its GI rules for products imported into the 15 countries of the EU. This is an action that has divided the European continent between those who want to capture and monopolize generic names versus those who believe that generic names, as well as trademarks, are protected both by laws and by years of marketing and development.

Internationally, in the WTO forum, the EU has made it a priority to extend protection for GIs beyond the carefully limited category of wine and spirits. This action could threaten the exports or production of a number of U.S. products, particularly cheeses such as mozzarella and parmesan, as well as other hundreds of other types of products. Every effort should be made to oppose the EU's actions and to create a coalition of countries that understand the consequences of extending GIs to an unprecedented number of products. Under no terms should the U.S. government agree to a trade-off between GIs and progress in the agricultural negotiations.

The so-called "non-trade concerns" also include topics such as animal welfare, consumer attitudes and fears (known as the precautionary principle), and the notion that the special characteristics of agriculture should permit the continued use of trade restricting measures or trade distorting subsidies. These "non-trade" issues mainly interest the EU and Japan.

We agree that the specific role of agriculture as a provider of public goods should be recognized, yet we strongly disagree with any attempt to use those concerns to prevent trade. The U.S. dairy industry does not oppose the idea that agriculture is a unique economic activity that merits different treatment. However, the real issue is the manner in which the objective is accomplished. Legitimate social, cultural and environmental goals are best accomplished through other programs that do not prevent trade. It is important that the United States prevent the inclusion of issues such as labeling, animal welfare and others in a final agreement if the provisions would result in further trade distortions.

Special and differential treatment for developing countries given in the form of restricting trade is an impediment to further trade and economic reform. The U.S. dairy industry is concerned that the current Harbinson proposal could allow developing nations to isolate themselves from global trade for the next 20 years. This goes in opposition to expanding exports and improving the economic well being of the Least Developed Countries (LDCs). These were major arguments expressed by the Administration for gaining Trade Promotion Authority. In addition to delaying the prospect of increased U.S. exports to these countries, this long-term protection will ensure that those countries miss out on many of the economy-building benefits of trade while the rest of the world profits from these measures.

The U.S. dairy industry rejects the concept of strategic products for developing countries. It also disapproves of permitting developing countries to maintain high levels of protection. Finally, under no circumstances should countries with large economies be allowed to be exempted from the trade reform process under the auspices of "developing country". For instance, although not as prosperous as the United States or the EU, Korea, Mexico and Brazil possess significant economics, neither of which should be classified as "developing". Moreover, despite living in a developing country, in many places, dairy producers are considered wealthy compared to the majority of their counterparts in the United States.

With regard to dairy, developing countries are right about the lack of benefits generated from the Uruguay Round. In fact, in dairy there are only two nations that have reaped the benefits of the Marakesh agreement - Australia and New Zealand. Neither the United States nor developing countries brought home real gains from opening their markets. The United States should look at alternatives to help LDCs establish competitive agriculture sectors as well as support their ability to access food supplies at reasonable prices. Nevertheless, protecting their market while we open ours will not accomplish the objective. The National Milk Producers Federation proposes that a large portion of whatever new access is gained during the Doha Round be reserved and given exclusively to developing countries.

Free Trade Area of the Americas (FTAA)

The U.S. dairy industry believes that a Free Trade Area of the Americas (FTAA) is long overdue, as history shows we have lost ground to our trade competitors who aggressively pursued and continue to pursue such activities. For years, the United States has failed to profit from the potential economic benefits that would arise from greater trade links with the Western Hemisphere countries.

The potential for export growth in Latin America is enormous. Every country in that region except Argentina, Uruguay, Costa Rica and Nicaragua is a net importer of dairy products. Of these exceptions, only the first two generate significant exportable surpluses. The region as a whole imports three-and-a-half times as much dairy products as it exports. And the United States produces more milk, cheese, milk powder, whey and lactose than the other combined 34 countries in the hemisphere.

Total cheese imports for Latin America approach a quarter of a billion pounds a year, more than a month's output from Wisconsin, the largest U.S. cheese producing state. Latin America imports more than a billion pounds of milk powder annually, and buys more than 150 million pounds a year of whey proteins. These are significant numbers.

Existing measures of per-capita consumption illustrate the potential demand for U.S. dairy products in a more open hemispheric trade environment. Annual dairy consumption in South America (excluding the large production bases in Argentina and Uruguay) averages 229 pounds per year. In Central America and the Caribbean, the average is 192 pounds. It is unrealistic to expect these countries to quickly achieve the levels of consumption in the United States and Canada, both around 585 pounds per year. However, it is realistic to see continuing growth as per capita incomes rise and begin to drive consumption to the levels that exist in Turkey, Pakistan or Russia (respectively, 321, 403 and 520 pounds per year). After all, Latin Americans use dairy products widely in their local diets and cuisine. Unlike Asian countries, where dairy products are rapidly building familiarity among non-traditional consumers, increased dairy demand by Latin American consumers is much more a matter of increased income and wealth, both factors that increased trade will foster.

More importantly, Canada, our largest trading partner, with whom the United States has concluded trade agreements in the recent past, will be a significant market should an FTAA eliminate its tariffs on U.S. cheese (245 percent) and butter (300 percent), as well as their tight quotas on other U.S. dairy products.

The dairy industry supports the U.S. goal of facilitating the process of ongoing hemispheric integration through trade. Furthermore, we support elimination of most, if not all, tariff and non-tariff barriers from the Arctic Circle to Tierra del Fuego, just as the North American Free Trade Agreement (NAFTA) has sought to do with the United States, Canada and Mexico.

The challenge will rest on negotiating an agreement that removes barriers within the hemisphere, but does not, as a consequence, leave the U.S. dairy industry vulnerable to the trade inequities that will remain in world dairy trade. Of particular importance to a balanced dairy sector agreement are the issues of rules of origin, third party export subsidies and the full inclusion of Canada.

Rules of origin is a fundamental concept of a regional trade agreement that dictates that economic benefits accrue exclusively to the countries within the region. Dairy suppliers from around the world continually explore ways to expand their shipments to the United States. Milk's versatility creates the opportunity for that expansion by its great variety of tradable products – almost 400 individual tariff lines of the HTSUS include significant proportions of milk and dairy components. In the absence of appropriate rules of origin, it will no doubt be tempting for non-party countries to attempt to transship their dairy products through participating countries.

NAFTA also includes a provision addressing rules of origin. For the purpose of determining origin, NAFTA allows for products to be "accumulated" from any of the participating countries, as long as all other relevant conditions are met (i.e., those relating to non-originating materials used in the production of the good undergoing a required tariff classification change, and the good satisfying any applicable regional value-content requirements). Although accumulation is included in NAFTA; its relevance is limited, since the agreement only has two parties. Accumulation would be a much more complicated issue in a free trade agreement covering many countries, such as the FTAA.

That is why NMPF believes it is vital that FTAA rules of origin do not allow for accumulation between the member countries. Were accumulation to be truly restricted to the participating member countries, this accumulation would be acceptable. However, determining the necessary logistics of such a process and providing proper monitoring would be virtually impossible, thereby providing no assurance that the products are not actually being transshipped from a third party.

If the rules of origin permit non-parties to transship dairy components into the U.S. market via FTAA partners, then we estimate that the quantity of these additional imports – above and beyond those that truly originate from FTAA members – could amount to as much as 4 billion pounds per year, on a milk equivalent basis, following full implementation of the FTAA. The negative impact of these additional imports on the U.S. dairy industry would be substantial. Milk prices received by producers would average up to $.60 per hundredweight lower and gross revenues received by U.S. dairy farmers would drop by as much as $1.2 billion per year. Several thousand dairy farms, mostly smaller family farms, would be forced out of business, and the industry would undergo consolidation.

Another key issue, the issue of export subsidies, must also be addressed in the FTAA. If the United States agrees to stop using subsidies to export dairy products to FTAA members, we must then ensure that our trading partners do not accept subsidized product from outside the hemisphere. If Brazil, for example, accepts subsidized product from the EU, while we agree not to use the Dairy Export Incentive Program (DEIP) to meet that subsidized competition in the Brazilian market, it will put us at a serious competitive disadvantage.

For example, in its most recent report to the WTO, the EU reported spending more than 100 times what the United States spent - $955 million versus $9 million. Such a statistic demonstrates why it is critical that FTAA members not accept subsidized dairy imports from non-FTAA parties if the United States is to agree not to provide its own subsidies to compete in FTAA member markets. In the absence of such provisions, a U.S. agreement not to subsidize into such markets will effectively deny the United States any significant gains from the agreement in terms of increased exports within the hemisphere. The costs to the United States in terms of increased dairy imports from FTAA members would therefore have no offsetting benefits and the agreement would be seriously detrimental to the U.S. dairy industry.

Finally, but most importantly, for the U.S. dairy industry the true economic value of Western Hemisphere trade cooperation is the inclusion of the Canadian dairy industry in any form of economic or trade integration. The U.S. dairy industry is united in agreement that a failure to bring Canada on board would substantially nullify any prospective net gains to closer regional integration.

In the U.S.-Canada FTA, in NAFTA and in its recent trade agreements with Chile and Costa Rica, Canada successfully kept dairy products off the bargaining table in order to preserve its supply-management regime. The real challenge for FTAA negotiators will be to find a way to bring the Canadian dairy industry into the agreement. If Canada succeeds in excluding its dairy sector, the U.S. dairy industry would find little reason to support an FTAA.

Following full implementation of the FTAA, we estimate that the United States would gain net dairy trade into Canada amounting to about 5 percent of Canada's commercial dairy market, equivalent to about 1 billion pounds of milk. This would boost milk prices received by U.S. producers by about $.15 per hundredweight and would increase gross revenues received by U.S. dairy farmers by over $300 million per year.

In the face of this significant potential benefit, unconfirmed press reports that the Administration is considering dropping parts of agriculture from the FTAA negotiations are alarming. Despite the substantial competition that the FTAA might bring from dairy suppliers in Argentina, Uruguay and maybe Brazil, we strongly support the FTAA for its ability to finally bring the Canadian dairy industry into the North America market global system.

Australia FTA

The commencement of the Australia FTA negotiations has alarmed U.S. dairy producers, as well as a wide range of large and small proprietary dairy processors.
Free trade agreements by definition are exceptions to the first and most fundamental article of the General Agreement on Tariffs and Trade – the principle that in its trade relations no country should treat one country more (or less) favorably than any other country. This is called the "most-favored nation" or MFN principle. An exception to that principle in the form of a bilateral or regional free trade agreement should be sought by the United States only when there is a clear and compelling argument that it is in our national economic interest. Such an argument is not evident in the case for an FTA with Australia, particularly in the sector of agriculture. Moreover, in the absence of any certainty on a favorable result on the U.S. Doha agenda, we have great apprehension that we will face a substantially unreformed global trade system while fully opening ourselves to a major competitor.

In 2001, the United States exported $0.3 billion worth of agricultural products to Australia and imported $1.8 billion from Australia. This six-fold difference in Australia's favor is likely to grow substantially, not decline, as a result of a free trade deal between the two countries. Virtually the same ratio of exports to imports applies in the dairy sector where Australia shipped $62 million to the U.S. and the U.S. sold only $6.8 million to Australia. In dairy, too, the ratio is for significant growth in Australia's favor under an FTA.

U.S. agricultural exports are limited in part by the size of the Australian market – with a population only 7 percent the size of the U.S. population (about 20 million), in part by the fact that Australia is a net exporter of many of the same farm products produced in the

U.S., and in part by the fact that Australia employs strict sanitary and phytosanitary barriers to prevent unwanted products from entering its market.

Eliminating U.S. dairy import tariff-rate quotas on imports from Australia, as a result of a U.S.-Australia FTA, without eliminating all global trade distortions in dairy, especially market access and export subsidies, would have a significant and negative impact on employment in the U.S. dairy industry. NMPF's economists have calculated that such an agreement would put at risk 1,170,000 jobs that are generated directly or indirectly by the milk production and dairy processing and manufacturing sectors of the U.S. dairy industry.

This employment figure represents employees directly involved in milk production and dairy product processing, the employment in industries supplying inputs to dairy farm operations and inputs in addition to milk to dairy processing and manufacturing establishments, and employment generated by dairy industry employee spending. Of the over 1 million jobs put at risk, NMPF calculates that by the ninth year of the agreement at least 13% of them, 150,000 jobs, would be lost due to displacement by Australian imports.

While the European Union continues to expand their Free Trade Agreements with developing countries (over 25 as of the beginning of this year), the United States is seeking an FTA with a country that is not only a large competitor of the U.S., but is also a direct competitor of most under-developed economies, as well. Farmers from developing nations have fought Australia's unfair trade practices in both the international and domestic markets. Making the Australia FTA a priority will hurt the poorest agricultural sectors in the world as well as the most vulnerable producers in the United States. By promoting the enrichment of the already rich nations such as Australia, the United States is doing a disservice to itself and to the advancement of the WTO Doha agenda.

In fact, a U.S.-Australia FTA that included dairy would likely undermine the eventual results of the Doha round negotiations by providing Australia with a substantial proportion of the gains in market access it could only hope to achieve through the far more complex and uncertain multilateral negotiations. Such an agreement with Australia would not only offer no net benefit to U.S. agriculture, it would also undermine the U.S. government's efforts to open markets around the world in a multilateral context. It would undoubtedly relieve much of the pressure on Australian negotiators to achieve a substantial result in the WTO, and thus leave the U.S. dairy market to be the sole outlet for Australia's expansion of milk and dairy product production. Throughout the United States, dairy producers are opposed to granting Australia more access to our markets, especially without first having acquired real offsetting export opportunities for the U.S. elsewhere.

Chile, CAFTA and Other Bilateral Agreements

With the above-mentioned exception of the U.S.-Australia Free Trade Agreement, the U.S. dairy industry supports all trade initiatives currently underway. We believe that such trade initiatives, particularly those within the western hemisphere, are clearly called for due to the potential economic benefit that would arise from greater trade links with the western hemisphere countries. That is why, in addition to supporting a Free Trade Area of the Americas that would include Canada, NMPF is a strong supporter of a clearly negotiated free trade agreement with Central America, as well as the recently-completed U.S.-Chile Free Trade Agreement.

To begin with, the U.S. dairy industry applauds the Administration on its completion of the U.S.-Chile and U.S.-Singapore FTAs, and encourages Congress to approve these mutually beneficial agreements. U.S. negotiators achieved a major victory when Chile agreed, as part of the Free Trade Agreement, to accept imported dairy products from dairy plants certified by the U.S. government. It took many years of effort by technical and regulatory officials at USDA to convince Chilean authorities of the thoroughness and integrity of U.S. government oversight. However, NMPF takes issue with the agreement's requirement that the Food and Drug Administration (FDA) create a separate list of companies approved to export to Chile.

We note that the procedures listed in the guidance document are quite similar to those implemented in 1997 by FDA to establish the list of approved European Union dairy exporters. In both instances, firms that seek inclusion on the FDA Federal Register Notice reference list must provide a collection of detailed information. Based on experience with the EU exporter list, the time required for the government to process this information has engendered delays of up to several months, preventing U.S. firms from being included on the reference list, and thereby stifling their export opportunities.

This requirement for the FDA to create a new list of approved exporters is needlessly burdensome on U.S. industry. Lists of approved exporters already exist and should be used for all free trade agreements the U.S. undertakes. Requiring U.S. companies to repeatedly register for the same opportunity creates unnecessary costs and barriers to trade.

As for agreements that remain under negotiation, we believe that a U.S.–Central America FTA (CAFTA) makes economic sense for the United States, as it would increase prosperity for these neighboring countries. Benefits to the U.S. dairy industry are clear, as Central America is a net importer of dairy products. In 2000, dairy imports to the five Central American countries from other countries amounted to $145.5 million. Dairy exports from the five countries to external destinations were just $3.7 million that year. In the year 2000, half of these imports were from North America, primarily the United States, 23 percent were from Oceania (New Zealand and Australia), and 16 percent were from the European Union. In the last three years, U.S. exports of milk powders and cheese to Costa Rica, El Salvador, Guatemala and Nicaragua grew steadily. We believe that even if the FTA brings a rise in domestic dairy production, we will help consumption to increase at a faster rate, resulting in a clear benefit for both the Central American and the U.S. dairy industries.

Eliminating tariffs on Central American imports of dairy products from the United States may stimulate some additional U.S. dairy exports by overcoming the advantages of export subsidies for EU products and undercutting prices from New Zealand and Australian exports. Similarly, providing duty-free treatment for U.S. imports to dairy products from the five Central American countries is not likely to have a significant economic effect on industries in the United States producing like or directly competitive products; nor upon consumers, provided that the liberalized access to the U.S. dairy market provided by the FTA is restricted to dairy products produced from milk and dairy ingredients that truly originate from those five countries.

As desired in the FTAA and discussed above, imposing specific rules of origin in order to mandate that all milk and dairy ingredients for which access to the U.S. market is liberalized must be manufactured from milk produced by cows in the five Central American countries themselves is a vital component the CAFTA must possess. In the absence of such rules of origin, dairy products and dairy ingredients produced in third countries, particularly New Zealand, Australia and member countries of the European Union, could easily be transshipped through Central America to benefit from the large difference in tariff treatment afforded products that will qualify for liberalized access to the U.S. market under a bilateral agreement.

As discussed in relation to the FTAA, it is important that CAFTA rules of origin do not allow for accumulation between member countries. Due to the nearly insurmountable task of establishing adequate monitoring devises to ensure that accumulation does not inadvertently permit third-party products to enter the U.S. duty-free, NMPF feels the most logical and prudent decision is to prohibit accumulation across the Central American countries.

Our main concerns with other bilateral agreements such as Morocco and the South African Customs Union are the issues of rules of origin, the EU's export subsidies, and general reciprocal access. NMPF is supporting these agreements on the basis that the elements sited will be carefully considered during the negotiations.

The National Milk Producers Federation encourages the U.S. government to focus on the WTO negotiations. We understand Ambassador Zoellick's objective of "competition on liberalization." If the Administration's desire is to pursue more Preferential Trade Agreements (PTAs) with other nations, we believe that this committee should have an important say on which PTAs the U.S. should pursue. As indicated by Ambassador Zoellick on several occasions, the European Union has concluded numerous agreements without jeopardizing its competitive advantage in the global market. Further trade reform can only be achieved in a multilateral context. Free Trade Agreements (FTAs) with competitive developed nations will only erode the U.S. agricultural industry's efforts to further reform the world's distorted agricultural trade structure.

Israel FTA

We would like to remind the House Agricultural Committee that the United States and Israel have not concluded their negotiations on the agricultural section of their FTA. As we all know, the 1995 U.S.-Israel Free Trade Agreement did not apply to trade in all products between the two countries. In fact, the United States and Israel signed an unusual five-year agreement on agricultural products. This accord expired in December 2001 and was extended for one year. Negotiations continued at a slower pace and have yet to resume progressing.

The U.S. dairy industry would benefit from the inclusion of dairy products in this agreement, but in a manner that provides reciprocal meaningful access between the U.S. and Israel. It is imperative that flaws of the original U.S.-Israel FTA be corrected during the negotiations once they resume. Israel is a small, but wealthy nation with a relatively high consumption of dairy products.

Although Israel's market access offer on agricultural products, including dairy, is a positive move on the part of Israel, this offer falls significantly short of U.S. dairy industry expectations, particularly on the cheese side. As the negotiations progress, we hope that the U.S. government will not soften its negotiating position with respect to the most important dairy products.

Overall, it is imperative that Israel's TRQ administration be immediately reexamined and improved. Our exporters have encountered numerous problems in filling TRQs and/or in developing a market for their products in Israel. The main obstacle seems to be Israel's licensing procedures. It is our understanding that Israeli officials have acknowledged that serious problems exist with the manner in which TRQs and import licensing are administered.

NMPF respectfully recommends that this agreement should not be treated as a low priority among U.S. negotiators, or simply as a political accord. The achievement of short-term objectives outlined above will benefit U.S. dairy exporters, while benefiting Israeli consumers. At the same time, adoption of longer-term goals will ensure that the U.S. will have a competitive advantage over other exporters.

Dairy Export Incentive Program (DEIP)

On a milk equivalent basis, the EU accounts for fully 72 percent of the subsidy allowances agreed upon in the Uruguay Round; the U.S., which produces two–thirds as much milk as the EU, accounts for just three percent of these allowances. Such heavy export subsidies drive down international prices, making U.S. dairy exports uncompetitive. With a renewal of the DEIP program, U.S. suppliers have some ability to compete.

However, we must openly state that perhaps even more important than the DEIP's impact on leveling the playing field, is the leverage it provides in negotiating the next agricultural agreement in the WTO. The U.S. dairy industry has stated repeatedly that it is quite ready to accept elimination of the DEIP program as part of an elimination of all agricultural export subsidies worldwide.

Therefore, contradictory though it may sound, to destroy export subsidies, we must use them. In this instance, that means extending the DEIP program and using it to the fullest extent that domestic market conditions warrant.

Yet, without advance consultation, the Administration announced in the President's recent commencement address at the Coast Guard Academy that the U.S. would no longer subsidize farm products to developing countries in the hopes that the EU would do the same. While we certainly laud the intent of the initiative – we ardently seek to eliminate all export subsidies in the Doha Round – its entire weight falls onto our industry, since the U.S. currently uses export subsidies only for dairy.

Developing countries in Southeast Asia and elsewhere have long sought U.S. dairy products both for our quality and to offset a reliance on the EU and Oceania. Sudden delisting of these destinations calls into question our reliability as a supplier, creates substantial difficulty in fully utilizing our WTO allocations, and *unilaterally* disarms U.S. leverage in a key part of the WTO modalities debate. Since developing countries were a key destination for dairy exports, the only suitable remedy would be to restore DEIP eligibility for a large number of the more developed destinations, or to add *developed* countries, such as Japan and the EU as DEIP-eligible destinations.

I appreciate the opportunity to testify before you today and will be pleased to answer any questions you might have.

Thank you.

Tom Camerlo